

VZCZCXRO4000
RR RUEHIK
DE RUEHVB #0135/01 0321603
ZNR UUUUU ZZH
R 011603Z FEB 06
FM AMEMBASSY ZAGREB
TO RUEHC/SECSTATE WASHDC 5637
INFO RUEHZL/EUROPEAN POLITICAL COLLECTIVE
RUCPDO/DEPT OF COMMERCE WASHDC

UNCLAS SECTION 01 OF 02 ZAGREB 000135

SIPDIS

SENSITIVE
SIPDIS

EUR FOR EUR/SCE

E.O. 12958: N/A

TAGS: [ECON](#) [ETRD](#) [ECIN](#) [EU](#) [HR](#)

SUBJECT: FREE TRADE PROPOSAL TOUCHES OFF STORM IN ZAGREB

ZAGREB 00000135 001.2 OF 002

¶1. (SBU) Summary and Comment: The European Union touched off an exaggerated, if predictable reaction in Croatia last Friday when it gave its support to the Stability Pact Free Trade Agreement for Southeast Europe. Seized upon by a press corps ever eager to stir up controversy and let political blood, the proposal was portrayed at best as an effort to stall Croatia's progress towards the EU and, at worst, an overt attempt to create a new Yugoslavia. The far right was quick to take the bait and rational voices were hard to hear among the din of political and nationalist grandstanding.

¶2. (SBU) Prime Minister Sanader reacted more deftly, appeasing party faithful by stating the obvious that any attempt to rebuild Yugoslavia was unacceptable, but leaving himself room for maneuver by saying that Croatia would support the creation of such a zone within the framework of the Central European Free Trade Agreement (CEFTA). Sanader has left himself a face-saving way out of this one, but will need help re-branding the proposal as being within the framework of CEFTA, which he can then sell as a concession to Croatia's demands. End Summary and Comment.

A Predictable Reaction

¶3. (SBU) Croatia's reaction to the EU's backing of a Southeast Europe free trade zone was not entirely unpredictable. An MFA contact told us that the GOC viewed the proposal as a draft agreement and so was caught by surprise when Enlargement DG Rehn endorsed it publicly. With EU membership the top government priority and optimistically predicted by 2009, many here questioned the utility of entering into an agreement that would be obviated so shortly after coming into force. Furthermore, Croatia, like Slovenia before it, is eager to leave its "Balkan" and "Yugoslav" past behind and take what many here view as its rightful and historical place among the nations of "Central Europe," so associations with its southern neighbors produce a predictably neuralgic reaction here. In this context, the government found itself at a loss to explain a proposal that it was actually fully aware of beforehand.

Current Web of Free Trade Agreements

¶4. (SBU) Croatia has maintained that any free trade agreement must be based on CEFTA. Croatia is a member of CEFTA and has bilateral free trade agreements with all the countries of the region. CEFTA, originally conceived to bring the Visegrad 10 closer to EU membership, is the victim of its own success, with Bulgaria, Romania and Croatia the only remaining members. With EU accession expected for Bulgaria and Romania next year, the organization would

essentially cease to exist, absent an enlargement. Until now, the criteria for CEFTA membership, which Croatia has been resistant to change, have been WTO membership and the existence of a Stability and Association Agreement (SAA) with the EU - points on which neither Serbia and Montenegro nor Bosnia and Herzegovina would qualify for membership. Our contacts here now say that Croatia will support a relaxation of these criteria, as well as possibly the most cumbersome aspect of CEFTA, which is that new members require parliamentary ratification of their membership applications among existing members.

If It Ain't Broke, Why Fix It?

15. (SBU) Many in Croatia contend that existing arrangements are sufficient for Croatia, particularly given what they hope is the short path to EU membership. Croatian businesses have clearly benefited from these agreements, with exports to Serbia alone up nearly 50% last year. Croatia would seemingly have the most to gain from a regional free trade zone, as Southeast Europe represents the best export markets for its products, which are only marginally competitive elsewhere. Yet there is an attitude that the current system works fine. A contact in a large agro-industrial producer here told us that his company, which is a large exporter, currently pays 1% duties in all of the countries of the proposed free trade zone, so that for them, this is only a question of politics. He conceded, however, that this might not be the case between the other members.

Sanader's Dodge

16. (SBU) An artful politician, PM Ivo Sanader reacted to the proposal by saying that Croatia would oppose any attempts to create a new Yugoslavia, but that his government would support the creation of a new free trade zone within the framework of CEFTA. This is actually the reiteration of a long-standing Croatian line on the idea of a regional free

ZAGREB 00000135 002.2 OF 002

trade zone and gives Sanader the room to claim victory among the more conservative elements here, but still enable Croatia to join an agreement. Clearly there is very little enthusiasm for this idea in Zagreb, but Sanader is also a realist and does not want to be seen as obstructing the EU's agenda for the region.
FRANK